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Person To Contact:

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Telephone Number:

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PLR-128432-08

Date:

December 19, 2008

Legend

Bonds

County

Date

District

Facility

State

Year

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Dear _____ :

This is in response to your request for a ruling that the District's sale of renewable energy certificates will not result in private business use of the Bonds within the meaning of § 141(b)(1) of the Internal Revenue Code (the "Code").

FACTS AND REPRESENTATIONS

The District has made the following representations. The District, a political subdivision of the State, provides electric utility service to retail customers in County. The District currently obtains most electricity needed to provide this service from District owned and operated facilities, including the Facility, a hydroelectric facility acquired in Year.

On Date, the District issued the Bonds. The District has used or expects to use \$a of the Bond proceeds on the District's electric distribution system. The remaining \$b of Bond proceeds are to be spent to replace or rehabilitate turbines, generators, governors and unit controls for each of the Facility's c electric generating units (the "Project"). Each turbine generator unit at the Facility presently has a d megawatt ("MW") nameplate rating. Once the Project is completed, the nameplate rating of each turbine generator unit is expected to increase to e MW, resulting in increased electrical output of an estimated f to g percent.

A number of states are now imposing mandatory compliance programs that require some or all electric utilities providing service within those states to demonstrate that a specified portion of their electric supplies are derived from renewable generating resources ("renewable portfolio standards"). Many states imposing such renewable portfolio standards allow utilities to meet these requirements by purchasing renewable energy certificates ("RECs") from renewable electric generating resources. RECs represent the environmental attributes of renewable energy, with one REC representing the attributes for one MW hour generated by a renewable energy resource. Additional purchasers of RECs include individuals and business entities in voluntary green programs.

The District expects that some or all of the h MWh/year of electric energy anticipated to be generated at the Facility on completion of the Project will give rise to RECs that qualify under one or more of the mandatory compliance or voluntary programs. The District expects to sell some or all RECs associated with the Facility to a nongovernmental person, or persons, for use in a trade or business under contracts with terms exceeding 3 years.

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The District's proposed contracts (the "Contracts") will require the purchaser to buy the lesser of the stated amounts of RECs or all the RECs associated with the Facility's generation of electricity for the periods specified in the Contracts. The Contracts for sale of RECs to nongovernmental persons will not entitle the REC purchaser to any electric energy from the Facility. The Contracts will provide that the District will have exclusive control over the Facility, its operations, and any decision regarding how or whether to operate the Facility. The District will be under no obligation to the purchaser to produce any renewable electricity or to operate its Facility at all or at any particular level. The Contracts will not give the purchaser of the RECs any direct or indirect voice in how any component of the Facility is to be operated or maintained.

LAW AND ANALYSIS

Section 103(a) of the Code provides that gross income does not include interest on any state or local bond. Section 103(b)(1) provides that § 103(a) does not apply to any private activity bond which is not a qualified bond within the meaning of § 141.

Section 141(a) provides that a private activity bond is any bond issued as part of an issue that meets either (1) the private business use test of § 141(b)(1) and the private security or payment test of § 141(b)(2), or (2) the private loan financing test of § 141(c).

Section 141(b)(1) provides that generally a bond issue meets the private business use test if more than 10 percent of the proceeds of the issue are to be used for any private business use. Section 141(b)(6)(A) provides that the term "private business use" means use (directly or indirectly) in a trade or business carried on by any person other than a governmental unit. For purposes of § 141(b)(6)(A), use as a member of the general public shall not be taken into account. Section 141(b)(6)(B) provides that, for purposes of § 141(b)(6)(A), any activity carried on by a person other than a natural person shall be treated as a trade or business.

Section 1.141-3(a)(1) of the Income Tax Regulations provides that the private business use test relates to the use of the proceeds of an issue, and, for this purpose, the use of financed property is treated as the direct use of proceeds.

Section 1.141-3(b)(1) provides that both actual and beneficial use by a nongovernmental person may be treated as private business use. In most cases, the private business use test is met only if a nongovernmental person has special legal entitlements to use the financed property under an arrangement with the issuer. In general, a nongovernmental person is treated as a private business user of proceeds and financed property as a result of ownership; actual or beneficial use of property pursuant to a lease, or a management or incentive payment contract; or certain other arrangements such as a take or pay or other output-type contract.

Section 1.141-3(b)(7)(i) provides that any other arrangement that conveys special legal

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entitlements for beneficial use of bond proceeds or of financed property that are comparable to special legal entitlements such as ownership, leases or output contracts (or other arrangements not relevant for this purpose) results in private business use. For example, an arrangement that conveys priority rights to the use or capacity of a facility generally results in private business use.

Section 1.141-7 provides special rules to determine whether arrangements for the purchase of output from an output facility cause an issue of bonds to meet the private business tests. Section 1.141-3 applies to determine whether other types of arrangements for use of an output facility cause an issue to meet the private business tests. Section 1.141-1(b) provides that an “output facility” means electric and gas generation, transmission, distribution and related facilities, and water collection, storage, and distribution facilities.

Section 1.141-7(b)(1) provides that the available output of a facility financed by an issue is determined by multiplying the number of units produced or to be produced by the facility in one year by the number of years in the measurement period of that facility for that issue. Section 1.141-7(b)(1)(i) provides that the number of units produced or to be produced by a generating facility in one year is determined by reference to its nameplate capacity or the equivalent (or where there is no nameplate capacity or the equivalent, its maximum capacity), which is not reduced for reserves, maintenance or other unutilized capacity. Section 1.141-7(b)(1)(iv) provides that if a limited source of supply constrains the output of an output facility, the number of units produced or to be produced by the facility must be determined by reasonably taking into account those constraints. For example, the available output of a hydroelectric unit must be determined by reference to the reasonably expected annual flow of water through the unit.

Proceeds of the Bonds are to be spent on the costs of the Project; that is, replacing or rehabilitating the generating units at the Facility, an output facility within the meaning of § 1.141-1(b). The Project is expected to increase the nameplate capacity of the generating units and thus, the available output within the meaning of § 1.141-7(b)(1). Although RECs are measured based on the quantity of renewable electricity generated, RECs do not increase or otherwise impact the nameplate capacity of a generation facility or the annual flow of water through a hydroelectric unit, and the sale of RECs does not affect the units of electricity that may be sold or entitle the purchaser to any capacity of the generators. We thus conclude that RECs are not output for purposes of § 141 and the rules under § 1.141-7 do not apply.

The rules under § 1.141-3 must also be examined to determine whether there is private business use. Under the Contracts, the purchaser of RECs associated with the Facility will receive no legal entitlements to use of the Project. The purchaser is obligated to buy an amount of RECs that is the lesser of that stated in the Contract or that based on the amount of renewable electricity actually generated by the Facility. The RECs

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themselves are a means to meet renewable portfolio standards and do not represent capacity or use of the Project. Under the Contracts, the District will have no obligation to the purchaser to produce any renewable electricity and the District will have exclusive control over the Facility and its operations. Thus the purchaser has no direct or indirect control of the operation, or any other special legal entitlement, of the Project under § 1.141-3.

CONCLUSION

Based on the foregoing, we conclude that the District's sale of RECs under the Contracts will not result in private business use of the Bonds.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter. Specifically, no opinion is expressed concerning whether the interest on the Bonds is excludable from gross income under §103(a).

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representative.

Sincerely,

Associate Chief Counsel
(Financial Institutions & Products)

By: _____
Johanna Som de Cerff
Senior Technician Reviewer
Branch 5

cc: